**BEFORE THE ILLINOIS COMMERCE COMMISSION**

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| Frontier Communications Corporation, Verizon Communications, Inc., Verizon North Inc., Verizon South Inc., New Communications of the Carolinas, Inc.<br><br>Joint Application for the approval of a Reorganization pursuant to Section 7-204 of the Public Utilities Act the Issuance of Certificates of Exchange Service Authority Pursuant to Sections 13-405 to New Communications of the Carolinas, Inc.; the Discontinuance of Service for Verizon South Inc. pursuant to Section 13-406; the Issuance of an Order Approving Designation of New Communications of the Carolinas, Inc. as an Eligible Telecommunications Carrier Covering the Service Area Consisting of the Exchanges to be Acquired from Verizon South Inc. Upon the Closing of the Proposed Transaction and the Granting of All Other Necessary and Appropriate Relief. | )<br>)<br>)<br>)<br>)<br>)<br>)<br>)<br>)<br>)<br>)<br>)<br>)<br>)<br>) | Docket No. 09-0268 |

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**BRIEF IN REPLY TO EXCEPTIONS OF**
**THE INTERNATIONAL BROTHERHOOD OF ELECTRICAL WORKERS,**
**LOCALS 21, 51, AND 702**

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**PUBLIC (REDACTED) VERSION**


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# I. Introduction

The International Brotherhood of Electrical Workers, Locals 21, 51, and 702 ("IBEW") represent more than 1,000 employees of Verizon North Inc., Verizon South Inc. (collectively "Verizon Illinois") and Frontier Communications Corp. ("Frontier") in Illinois. IBEW Exh. 1.0, 1:11-12. IBEW opposes the proposed transaction between Verizon Communications Inc. ("Verizon") and Frontier that would transfer Verizon Illinois (along with Verizon's landline operations in 13 other states)[1] to Frontier – a transaction that would more than triple the size of Frontier.

IBEW strongly supports the Proposed Order issued by ALJ Tapia. The Proposed Order reflects a thorough and well-reasoned analysis of the evidence in this proceeding and properly applies that analysis to the statutory standards for the approval of this type of transaction.

The Public Utilities Act requires the Illinois Commerce Commission ("Commission") to make seven specific findings. The Proposed Order correctly found that the Commission cannot make all seven of those findings based on the evidence before it. In particular, Frontier fails to meet at least two of these criteria: the effect of the proposed transaction on the financial condition of Verizon Illinois and the ability of Verizon Illinois to provide adequate, safe, reliable, efficient, least-cost service.

IBEW's opposition is based on one over-arching concern that is accurately reflected in the Proposed Order: Frontier is not financially fit to own and operate Verizon's landline operations, including Verizon Illinois. As the ALJ correctly found, a lack of financial fitness cannot be cured or subject to a compromise – it simply renders the applicant unfit to assume the

[1] The entire group of Verizon service areas proposed to be transferred to Frontier are collectively referred to as Verizon Separate Telephone Operations, or VSTO. Tr. 406:13-20. Some of the evidence also refers to these areas as Spinco.

responsibility for serving more than half a million citizens of Illinois with an essential public service. In theory, of course, it is possible to restructure a transaction to better enable an applicant to be financially viable, but both Frontier and Verizon have emphatically testified that they will not restructure the transaction – and their Brief on Exceptions (cited herein as "Joint Applicants' BOE") does nothing to alter that position. Thus, the Commission must rule on the transaction that is in front of it – and that transaction would not create a financially viable utility holding company.

In addition, there are strong indications that the quality of service would be harmed if Frontier were permitted to acquire Verizon Illinois. The ALJ properly found that Frontier's record of service quality performance in other jurisdictions is questionable. She is correct that there are reasons to believe that Frontier will not be able to maintain Verizon's current level of service quality, let alone improve on that level of performance.

Thus, the Proposed Order correctly concluded that the proposed transaction fails at least two of the statutory criteria for approval of this transaction. The Commission, therefore, must deny the Application.

## II. Reply to Staff Exceptions 1, 2, and 3

Staff Exceptions 1, 2, and 3 are inter-related and address the Proposed Order's findings and conclusions about Frontier's financial condition.[2] The essence of Staff's argument is that the Proposed Order errs by focusing on the parent company's financial condition rather than the impact of the proposed transaction on the Illinois operating utilities: Verizon North and Verizon South.

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[2] IBEW does not take a position on Staff Exceptions 4 and 5.

Staff's argument, however, contains two fatal flaws. First, Staff fails to acknowledge that the proposed transaction will have a serious adverse impact on the credit rating of Verizon North and will impair that entity's ability to raise capital.

Specifically, on the day this transaction was announced, Moody's Investors Service placed the debt of Verizon North Inc. – the Verizon subsidiary serving more than 500,000 lines in Illinois[3] – on review for possible downgrade. Specifically, Moody's stated:

> As part of the transaction, VZ-Spinco will issue approximately $3 billion of new debt, while it is anticipated that $250 million of existing debt at the Verizon entities to be acquired will remain in place post-merger, although the amount may be up to $425 million, depending on the final timing of the merger closing. As a result Moody's has also placed the A3 senior unsecured debt ratings of Verizon – Northwest, North, and West Virginia on review for a possible downgrade, as it is unlikely that the post-merger entity will be rated at that level.

Frontier Exh. 5.3, p. 1 (emphasis added).

Thus, contrary to Staff's argument (which fails to acknowledge, let along discuss, the Moody's rating action), one of the major rating agencies recognized that the current investment-grade bond rating of Verizon North would be in jeopardy if Frontier acquires the company. It bears repeating that Verizon North is the entity that provides service to more than 95 percent of Verizon's customers in Illinois. The evidence of record unequivocally shows that the proposed transaction would have a negative impact on Verizon North's creditworthiness.

This highlights the second fundamental problem with Staff's argument (and with the proposed transaction). Regardless of the impact the transaction may have on Frontier (and IBEW submits the ALJ is correct that the impact on Frontier is far from beneficial), there is no question that the Verizon subsidiaries' financial condition would be substantially harmed by the proposed transaction. Whether the subsidiaries raise capital on their own – as Verizon North has

[3] Tr. 138-139. Verizon South serves fewer than 30,000 access lines in Illinois. Id.

done with the outstanding debt discussed by Moody's – or rely on the parent company for capital, the subsidiaries' credit ratings and their ability to raise capital are closely tied to the parent company's financial condition. There is no question that Frontier's financial condition – either before or after the proposed transaction – is substantially worse than Verizon's and that Frontier's ability to raise capital is seriously impaired as compared to Verizon. See IBEW Main Brief pp. 4-15 and Proposed Order pp. 29-33.

Moreover, Staff's position in its Brief on Exceptions is directly contrary to the testimony of its own witness, Ms. Phipps, who testified: "Frontier is the only source of external capital for the New Frontier ILECs. Therefore, the New Frontier ILECs' ability to raise external capital on reasonable terms depends on Frontier's ability to raise external capital on reasonable terms." Staff Exh. 3.0, 2:38-41. As Staff's witness recognized, the creditworthiness of the subsidiaries is directly tied to the creditworthiness of the parent. Changing the parent company from Verizon to Frontier will have a dramatic change in the subsidiaries' credit standing. Ms. Phipps again addressed this point in her testimony, stating: "Verizon's credit ratings are five to six notches higher than Frontier's ratings. As such, it will be more challenging for Frontier to raise capital for the New Frontier ILECs than it would be for Verizon." Id., 7:147-150.

In summary, Staff Exceptions 1, 2, and 3 are incorrect. First, Verizon North's credit rating will be seriously and adversely affected by the proposed transaction. Second, as Staff's own witness testified, the ability of Verizon North and Verizon South to raise capital will be directly and inextricably tied to the credit rating of their parent company – and that credit rating will be significantly worse if Frontier is permitted to own the Illinois operating companies.

# III. Reply to Department of Defense / Federal Executive Agencies ("DoD/FEA") Exception 1

IBEW's response to DoD/FEA Exception 1 is contained in IBEW's reply number 7 to Verizon / Frontier exceptions. IBEW does not take a position on DoD/FEA Exception 2. IBEW would note, however, that the DoD/FEA Brief on Exceptions fails to incorporate any "suggested replacement statement or finding" as required by the Commission's regulations, which makes it difficult to understand specifically how that party proposes to modify the Proposed Order. Ill. Admin. Code § 200.830(b).

# IV. Reply to Verizon / Frontier Exceptions

## A. The Verizon / Frontier Brief on Exceptions Does Not Comply with the Commission's Regulations

Verizon and Frontier ("Joint Applicants") filed a joint Brief on Exceptions that fails to comply with the Commission's regulations in two important respects.

First, Section 200.830 of the Commission's regulations requires that "exceptions … must be specific and must be stated and numbered separately in the brief." Joint Applicants' Brief on Exceptions contains no such numbering and seems to make the same arguments multiple times. IBEW has attempted to discern the fundamental exceptions made by Joint Applicants. If IBEW has missed any exceptions, it is due to the non-compliant nature of Joint Applicants' Brief on Exceptions, not to IBEW's agreement with any positions stated therein.

Second, Joint Applicants make several statements that sound factual in nature but contain no citation to record evidence. The Commission, of course, cannot rely on any evidence outside of the record, and the regulations explicitly state that any statements of fact in a Brief on Exceptions must include citations to the record. Ill. Admin. Code § 200.830(e). Specific instances where Joint Applicants attempt to rely on extra-record information include the following:

- Pages 6-7: "*Indeed, the parties' Merger Agreement requires Verizon to create replicas of the operational support systems it uses for its own operations and then to actually use those replicated systems to operate Verizon North and Verizon South for at least sixty days prior to the closing of the Transaction. Frontier negotiated that provision (which Verizon has already spent hundreds of millions of dollars to implement) precisely to avoid the types of service problems experienced by other acquirers in past transactions.*"
  There is no citation to the record for this statement. In fact, there is no evidence in the record concerning the amount of money that Verizon has spent on implementing this provision. It seems highly unlikely that this effort would require the expenditure of "hundreds of millions of dollars" since Verizon testified that FairPoint Communications and Hawaiian Telcom were able to build completely new systems from scratch for "tens of millions of dollars." Verizon Exh. 7.0, 19:383-384.

- Page 7: "*And as explained below, an independent third party recently certified that the pre-production testing of the systems was 100% successful …*"
  There is no citation to the record for this statement. The record contains no information about the results of third-party testing and, as far as IBEW can discern, there is no explanation at any later point in the Brief on Exceptions.

- Page 21: "*Verizon has made clear that it will not deploy broadband in Illinois beyond its current levels.*"
  There is no citation to the record for this statement. In fact, Frontier witness McCarthy stated only that Verizon had no broadband deployment plan for Illinois. From the lack of a planning document, Frontier "assume[d] that there is no further plans … to invest in broadband in the state." Tr. 442. But there is no evidence that Verizon "will not deploy broadband in Illinois" as the Joint Applicants' brief alleges.

- Page 32: "*Verizon South and Verizon North … will remain as freestanding operating companies …*"
  There is no citation to the record for this statement and the statement is not accurate. Verizon North and Verizon South are not "freestanding" entities; they rely to a great extent on services provided by other Verizon affiliates, including such essential services as billing, call center operations, ordering, provisioning, 911 services, and network operations, among others. See, e.g., Tr. 95-96, 100 (911 services reliant on affiliated operations in West Virginia); Tr. 151-152 (billing, ordering, and provisioning reliant on affiliated operations in Indiana); Tr. 163-164 (network operations performed by an affiliate in Texas).

- Page 34: "*The replicated systems will be put into production on April 1, 2010, and the above conditions are already being implemented.*"
  There is no citation to the record for these statements. There is no information in the record concerning any actual testing or reporting concerning those systems.

- Page 49: Footnote 136 contains a reference to a publication that was not cited by any witness in the case and is not contained in the record.

- Page 57: *"Verizon South is quite small – it serves only 19,000 access lines …"*
  There is a citation to the record for this statement, but the documents cited do not contain this information. In fact, Verizon's witness stated that Verizon South serves closer to 30,000 lines in Illinois. Tr. 139.

- Page 57: *"[B]ased on Staff's analysis, only about 1,140 customer lines are out of compliance."*
  There is no citation to the record for this statement. To the best of IBEW's knowledge, neither Staff nor any other party quantified the number of lines that are out of compliance with section 13-517.

All of these statements that either rely on documents outside the record or that do not contain citations to the record must be disregarded by the Commission. Alternatively, if the Commission wants to reopen the record and hold additional hearings to consider these alleged facts, then IBEW respectfully submits that other information that has become available after the close of hearings also should be considered. Such information could include 2009 financial results for Frontier and VSTO,[4] modifications to the agreements between Verizon and Frontier that include a new $105 million payment to Verizon at closing,[5] the terms and conditions of Frontier's new revolving credit agreement,[6] the terms and conditions of two series of notes that Frontier announced it would issue to fund a portion of this transaction,[7] and the Federal Communications Commission's National Broadband Plan.[8]

[4] Frontier filed a Form 8-K with the U.S. Securities and Exchange Commission on March 24, 2010, that contains summary financial statements for Frontier and VSTO on an individual and combined basis for 2009. Obviously, that information is not in the record of this case.
[5] The disclosure of this new payment is made in the Form 8-K that was filed on March 24, 2010.
[6] The disclosure of this new agreement is made in the Form 8-K that was filed on March 24, 2010.
[7] The disclosure of the existence of these notes, but no information about their terms and conditions, is made in the Form 8-K that was filed on March 24, 2010.
[8] The Federal Communications Commission announced its National Broadband Plan on March 16, 2010. While the Commission could take administrative notice of the plan itself, given the timing of the FCC's publication of the plan, it was not possible to evaluate the effects of the plan on Frontier, VSTO, Verizon North, or Verizon South on the record in this case.

## B. Specific Replies

### Reply 1: The Proposed Order is Not an "Outlier"

Joint Applicants' lead argument is that the Proposed Order is an "outlier" because other state commissions have approved the proposed transaction. This argument is both irrelevant and misleading.

It is irrelevant because this Commission must decide the case based on Illinois law and the evidentiary record in this case. What another state does with a different statutory framework and different evidence has no bearing on this Commission.

Moreover, the argument is misleading because five of the six state commissions that have decided this case approved unanimous settlements or uncontested Staff recommendations. Thus, only one state – Ohio – has issued a decision based on a fully developed record in a contested proceeding.[9]

In addition to Illinois, there are two other contested proceedings that have been briefed and are awaiting commission decisions: Washington and West Virginia. Further, the Federal Communications Commission is still conducting discovery and has not yet indicated the procedure or timeline it will use to review the proposed transaction.

In short, the Proposed Order is not an "outlier." Illinois is one of four states that are involved in contested, on-the-record proceedings. One of those cases has been decided; three have not been decided.

[9] As Joint Applicants note in their Brief on Exceptions, the labor unions in that case have asked the Public Utilities Commission of Ohio to rehear the matter and reopen the record. That request is pending as of the date of this brief.

### Reply 2: Frontier Has a High-Risk, Unsustainable Business Model and Verizon Knew It.

The ALJ correctly found that Frontier's business model is not sustainable and that the company's finances are inadequate to assume ownership of Verizon North and Verizon South. Proposed Order pp. 29-33.

The Proposed Order's findings are fully supported by the record. IBEW demonstrated, using Frontier's own financial information, that Frontier consistently pays out far more to shareholders than the company earns. Those payments to shareholders also greatly exceed the amount that Frontier invests in its infrastructure. Indeed, in most years Frontier pays twice as much money to stockholders as it reinvests in its business. And in recent years, Frontier has been paying out to stockholders almost three dollars for every dollar that the business earns.

Specifically, from 2004 through 2008 Frontier paid $2,984,000,000 to its stockholders, but it earned net income of only $1,017,000,000 during that same time. IBEW Exh. 1.0, Sch. 4. That is, almost $2 billion left the company – money that was paid to stockholders over and above what the company earned by using stockholders' assets.

This trend continued in the first half of 2009 when Frontier paid its stockholders $156 million but earned only $65 million in net income. IBEW Exh. 1.0, 19:353-354. This represents a payout of 240% of net income. Id.

Moreover, Frontier also pays out far more to stockholders than it reinvests in its infrastructure. Frontier's Chief Operating Officer, Mr. McCarthy, acknowledged that during a four-year period from 2005 through 2008 Frontier made capital investments of $1.1 billion, but it paid stockholders more than $2.1 billion during that same time. Tr. 457-459.

The record also demonstrates that Frontier is headed for a crash: within two or three years, it will run out of retained earnings and will no longer be able to pay dividends in excess of its earnings. IBEW Exh. 1.0, 22:410 and Sch. 6. This would require Frontier to drastically reduce its dividend – by 60% or more – and then come up with a new strategy for providing value to its stockholders.

Not only are these facts uncontested, Verizon itself knew of them and relied on them to try to negotiate a better deal with Frontier. In an allegedly confidential e-mail message, the head of Verizon's negotiating team, Stephen Smith, wrote on April 19, 2009:

> **<<<BEGIN CONFIDENTIAL & PROPRIETARY** [redacted] **END CONFIDENTIAL & PROPRIETARY>>>**

IBEW Exh. 1.0, 24:447-454.

Mr. Smith submitted rebuttal and surrebuttal testimony in this case and failed to even mention, let alone try to explain or rebut, his opinion of Frontier's financial condition.

The ALJ properly found that Frontier's approach to business is not sustainable and is not in the public interest. Her findings are fully supported by the record evidence, including Verizon's allegedly confidential opinion of Frontier's financial condition.

### Reply 3: Verizon North's Creditworthiness Will Be Severely Harmed By the Proposed Transaction

Verizon and Frontier discuss at some length, and in several locations, the need to evaluate this transaction based on its impact on Verizon North and Verizon South. See, e.g., Joint Applicants' BOE pp. 7, 22-23, 40-42, and 45-46. But there are two important facts they never mention.

First, as IBEW discussed in response to Staff Exceptions 1, 2, and 3, there is unequivocal evidence that Verizon North's credit rating will be downgraded from its current investment-grade status to something much less than investment grade. Thus, if the Joint Applicants believe that the impact on Verizon North's creditworthiness is the appropriate statutory standard, then there is no question that the transaction will have a decidedly negative impact, as the ALJ found.

Second, the Joint Applicants conveniently ignore the fact that their own witness refused to assess the transaction's impact by evaluating Verizon North and Verizon South. In discussing the statutory standards, Verizon witness McCallion testified: "the Reorganization will not significantly impair Frontier's abilities to raise necessary capital on reasonable terms or to maintain a reasonable capital structure (220 ILCS 5/7-204(b)(4))." Verizon Exh. 6.0, 5:110-112 (emphasis added). During cross-examination, Mr. McCallion was specifically questioned about this statement to determine whether he meant to refer to the transaction's impact on Frontier's financial condition or its impact on Verizon's Illinois operating companies. Mr. McCallion succinctly testified that, in his mind, the relevant question was the impact of the transaction on Frontier, not on Verizon Illinois:

> Q. Now, in the fourth bullet which begins on line 110, you talk about the impact on Frontier's ability to raise capital. Is that your understanding, that the standard, if you will, is addressed to Frontier's ability to raise capital as opposed to an impact on Verizon Illinois' ability to raise capital?
>
> A. That's my understanding.

Tr. 161.

But now that the ALJ has found that the transaction would have an adverse impact on Frontier's financial condition, the Joint Applicants are disavowing their own witness and are trying to adopt a completely different theory. Now they argue that the ALJ erred – erred by following the approach advocated by Verizon's own witness – and that the only relevant financial impact is the impact on Verizon's Illinois operations.

As discussed above, however, if that is the appropriate level of analysis, then this transaction must fail. There is no question that this transaction would cause serious harm to Verizon North's credit rating (as Moody's already has concluded) and its ability to raise capital.

### Reply 4: The Terms and Conditions that Wall Street Lenders Will Place on Frontier are Unknown, and the Commission Cannot Rely on Those Lenders to Protect the Public in Illinois

Frontier must issue approximately $3.3 billion in new debt to finance this transaction. Frontier Exh. 5.0, 28:709-710. As of the close of the record, Frontier had not obtained a commitment for this financing and could not state the terms and conditions under which Wall Street investment banks would be willing to lend these funds to Frontier. Tr. 437.

The ALJ correctly found that this new debt would be a burden to Frontier and would greatly increase the risk of the proposed transaction. Proposed Order pp. 30-32.

Frontier asserts in various places in its exceptions that not only would this new financing not be a burden to Frontier, but that it actually would help the company. For example, Frontier states that the "new debt will be more than offset by substantial incremental revenues and cash flows from the properties it is acquiring" from Verizon and that "Frontier unquestionably has access to capital on reasonable terms." Joint Applicants' BOE, pp. 9 and 43. Frontier even goes so far as to say that it would be "imprudent" to have obtained a financing commitment. Id., p. 51. Apparently Frontier believes that the "prudent" course of action is to put a blindfold on this Commission – assert that the financing is not a problem, but provide the Commission and parties with no information about the interest rates and other terms and conditions that Wall Street lenders will impose on the company.

Rather incredibly, Frontier even asks this Commission to cede its authority to the unknown investment bankers. Thus, Frontier states: "the fact that Frontier 'must secure financial backing from a lender' provides 'additional assurance' that the financial aspects of the transaction 'will be given prudent review.'" Id.

IBEW believes it is unprecedented for a transaction of this magnitude to be filed – let alone decided – without knowing the source of the financing and the specific terms and conditions of that financing. The fact that some group of investment banks must provide more than $3 billion in capital to Frontier – and that Frontier has so far been unwilling or unable to obtain such financing – should lead the Commission to question Frontier's financial soundness; it should not give the Commission comfort that some unknown group of lenders will eventually present Frontier with a set of unknown terms and conditions.

Indeed, experience in recent years with similar transactions provides further evidence of investment banks' failure to accurately assess the financial risks of this type of transaction. Investment banks funded Verizon's sale of Hawaiian Telcom to the Carlyle Group, but Hawaiian Telcom went bankrupt within two years after the transaction closed. IBEW Exh. 1.0, 56-57:1046-1060. Similarly, investment banks funded Verizon's sale of its landline business in Maine, New Hampshire, and Vermont to FairPoint Communications, but FairPoint went bankrupt less than two years after the transaction closed. Id., IBEW Exh. 3.0, 17:323-327.

Rather than providing assurances about the financial soundness of a business, the Commission should be very concerned that Frontier has been unwilling or unable to obtain financing for the deal and that the terms and conditions of any such financing are unknown. Investment banks will try to protect their own interest (and do not always succeed at doing even that), often at the expense of the interests of consumers and the public.

IBEW submits, therefore, that the Commission cannot approve this transaction based on the record before it. The Commission cannot let Wall Street dictate the terms and conditions under which Frontier will have to operate or let Wall Street be the sole arbiter of the effect of this transaction on the financial condition of Frontier, Verizon North, and Verizon South. The Commission cannot simply assume that investment bankers will be looking out for the best interests of Illinois consumers; indeed, exactly the opposite might be true.

### Reply 5: Frontier's Continued Reliance on 2008 Financial Data is Unreasonable and Grossly Misleading

On pages 44-45 and again on pages 48-50, Joint Applicants cite numerous financial figures as if they were facts. But in reality, the numbers cited are meaningless: they reflect what would happen if you took Frontier's and Verizon's <u>actual 2008 results</u> and projected them forward to 2013. In its actual presentation to the investment community on the day of the merger, Frontier properly called its leverage ratio "net debt / '08 EBITDA." Frontier Exh. 5.1, p. 15. It is not a projection of anything and should not be treated as such.

If one were interested in trying to estimate the actual earnings and cash flow of the new company, it would be necessary to use the companies' results from 2009 and project them forward. Those actual results were recently filed with the Securities and Exchange Commission.[10]

Even without a full year of results, however, there is no question that Frontier and VSTO's results during 2009 were vastly different from their results in 2008. During the hearings, Frontier's results for the first nine months of 2009 were made part of the record. IBEW Exh. 10.0. The record also contains VSTO's results through the first six months of the

[10] Frontier filed a Form 8-K with the U.S. Securities and Exchange Commission on March 24, 2010, that contains summary financial statements for Frontier and VSTO on an individual and combined basis. Frontier had previously reported its results (Frontier Communications Corp. Form 10-K, Annual Report for the Year Ending December 31, 2009, filed with the U.S. Securities and Exchange Commission on February 26, 2010), but to the best of IBEW's knowledge, the March 24 filing was the first report of VSTO's results for 2009. Obviously, neither the February 26 report nor the March 24 report are part of the record in this case.

year. Frontier Exh. 5.10. For example, comparing the first nine months of 2009 with the same period in 2008 shows that Frontier's revenues declined by 5.5 percent. IBEW Exh. 10.0, p. 4.[11]

In its Brief on Exceptions, Frontier continues to rely on its seriously outdated and meaningless "projections" that use 2008 actual results, then bootstraps onto those 2008 results the synergy savings Frontier hopes to achieve by 2013 – five years later. Interestingly, in its allegedly confidential financial projections – which Frontier did not provide as part of its testimony – Frontier projects that its revenues, expenses, cash flows, earnings, and other important financial measures will be very different in 2013 than they were in 2008. For example, between June 30, 2008 and June 30, 2009, VSTO lost more than 11 percent of its access lines, Frontier's net income declined by 37% and VSTO's net income declined by 29%. IBEW Exh. 1.0, 32-33:588-611. There is absolutely no basis for assuming that 2008's actual results will be representative of the conditions Frontier will face immediately after closing, let alone in 2013.

In summary, Frontier's continued reliance on the outdated financial information based on 2008 results must be rejected. The ALJ properly rejected the use of such information in the Proposed Order. That information is out of date, does not represent Frontier's financial condition today let alone after closing, and cannot be relied upon to draw any reasonable conclusions about Frontier's financial condition now or post-closing.

### Reply 6: The Proposed Transaction is Not Similar to the CenturyTel – Embarq Transaction

On page 31 of their Brief on Exceptions, Joint Applicants allege that this transaction is similar to the CenturyTel-Embarq transaction. Apparently, they base this statement on a comparison of the number of access lines involved.

[11] The exhibit shows Frontier's revenues for the first nine months of 2008 were $1.690 billion. For the first nine months of 2009, revenues fell to $1.597 billion, a decline of 5.50%.

What Joint Applicants fail to understand, however, are the numerous ways that this transaction differs from CenturyTel-Embarq. Two factors in particular stand in stark contrast to the proposed Verizon-Frontier transaction: (1) Both Embarq and CenturyTel had investment-grade credit ratings;[12] (2) CenturyTel did not make a cash payment to Embarq and did not have to issue any additional debt;[13] and (3) CenturyTel acquired Embarq in its entirety – all of the employees, affiliates, computer systems, working capital, inventory, and facilities became a wholly owned subsidiary of CenturyTel.[14] There was no need to separate anything, there were no risks associated with replicating computer systems, developing new systems, realigning employees, creating new operations centers, replacing inventory, or any of the numerous integration challenges that face Frontier.

Thus, while the size of the two transactions is similar, the structure of the transactions – and their financial impacts – could not be more different.

### Reply 7: Frontier's Proposed Broadband Plan for Illinois is Inadequate

On pages 1 and 21 of their Brief on Exceptions, Joint Applicants allege that Frontier will bring broadband to "100,000 unserved and underserved households" in Illinois. Similarly, DoD/FEA cites to Frontier's broadband commitment as a reason why the proposed transaction should be approved. DoD/FEA Brief on Exceptions p. 4.

Joint Applicants do not define "underserved." Under Frontier, Illinois faces the very real prospect of <u>every customer</u> in Verizon's service area being "underserved" because Frontier is committing to deploy service at a speed of only 1.5 megabits per second. Tr. 404-405.[15] In contrast, the FCC's National Broadband Plan sets a national goal of a minimum broadband speed

[12] *CenturyTel, Inc. and Gallatin River Communications, LLC d/b/a CenturyTel of Illinois, Joint Application for approval of reorganization pursuant to Sections 7 203 and 7-204 and for other relief*, Docket No. 08-0645 (Ill. C.C. Mar. 25, 2009), Order p. 6.
[13] <u>Id.</u>, p. 3.
[14] <u>Id.</u>
[15] In addition, Frontier defines "broadband" as being any speed over 1 megabit per second. Tr. 494

of 4 megabits per second with at least 100 million households having access to 50 megabit per second service by 2015 – just two years after Frontier hopes to provide only 85 percent of its Illinois customers with 1.5 megabit per second service. Moreover, Frontier has no plans whatsoever to bring higher-speed service to Illinois, such as the fiber-to-the-home service that Verizon currently provides in several states. IBEW Exh. 2.0, 45:842-843.

Moreover, Frontier does not explain why its commitment to Illinois of $40 million of capital spending on broadband over 3.5 years is either reasonable or sufficient to address the needs in this state. Frontier Exh. 13, p. 8. With 573,000 access lines (Joint Applicants BOE p. 21, n. 38), that amounts to less than $20 per year per access line.[16] By way of comparison, Frontier committed to capital spending of at least $110 per access line per year in Ohio.[17] Even if Frontier's spending on broadband is added to Verizon's level of capital spending in Illinois[18] (and there is no commitment for Frontier to continue spending at that level), Frontier still would be spending less in Illinois than it has committed to spend in Ohio.

### Reply 8: IBEW Does Not Have a "Narrow Parochial Interest"

The Joint Applicants attempt to demean IBEW's participation in this case by characterizing its interest as a "narrow parochial interest." Joint Applicants' BOE p. 17. IBEW finds this characterization offensive and grossly inaccurate.

IBEW is participating in this case because of a serious concern about the financial condition of a company that wants to become the employer of hundreds of its members in Illinois. An employer in financial trouble not only has a monetary effect on those who work for the company (jeopardizing wages, pensions, health insurance, and other benefits), but also can

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[16] ($40 million / 3.5 years) / 573,000 lines = $19.95 per line per year.

[17] *In the Matter of the Joint Application of Frontier Communications Corporation, New Communications Holdings, Inc., and Verizon Communications Inc. for Consent and Approval of a Change in Control*, Case No. 09-454-TP-ACO (Pub. Util. Comm'n of Ohio, Feb. 11, 2010), Order p. 8.

[18] The allegedly confidential capital spending by Verizon in Illinois can be found in Frontier Exh. 5.0, 70:1731.

result in deferred maintenance, inadequate plant replacement and upgrade practices, downsizing of the workforce, and other practices that affect worker and public safety and the reliability of service.

IBEW does not expend its resources just for fun and it is not participating in this case because of some "narrow parochial interest." Rather, IBEW is genuinely concerned about the impact on its members and the public they serve if Frontier becomes the second largest local exchange carrier in Illinois. The ALJ properly shares that concern.

IBEW does not undertake such representation lightly and it has participated in telecommunications merger proceedings only rarely. Of particular note, it participated in the Verizon-FairPoint merger proceedings in 2007 and early 2008. The New Hampshire Public Utilities Commission, for example, found IBEW's participation (in conjunction with the Communications Workers of America) to be particularly valuable, stating: "Among the key participants in this protracted proceeding have been the two labor unions that represent Verizon's highly experienced workforce in the three states. Their skepticism, and the evidence they produced, raised important questions about the economics of the transaction. Although they did not endorse the settlement agreement, in our judgment the Labor Intervenors' participation was key to the improved outcome."[19]

IBEW has brought the same level of professionalism and expertise to this case (and, in fact, the same counsel and financial expert) as it did to the Verizon-FairPoint cases. It has not done so to protect a "narrow parochial interest" but to ensure that the people who work for Verizon in Illinois, and the public they serve, will not be harmed by the proposed transaction. Unfortunately, and as the ALJ correctly found, that would not be the case as the transaction is

[19] *Verizon New England, Inc., Bell Atlantic Communications, Inc., NYNEX Long Distance Co., Verizon Select Services, Inc. and FairPoint Communications, Inc., Petition for Authority to Transfer Assets and Franchise*, 2008 N.H. PUC LEXIS 8, *148-149; 264 P.U.R.4th 185 (N.H. Pub. Util. Comm'n 2008).

presently structured. The transaction is too risky, and Frontier is too financially unstable, for the transaction to be in the public interest. The Commission, therefore, should adopt the Proposed Order and reject the proposed transaction as it presently exists.

IBEW would note that this is precisely the action taken by the Vermont Public Service Board on the Verizon-FairPoint transaction.[20] As a result of that commission's rejection of the transaction as presented to it, Verizon and FairPoint negotiated a substantially revised transaction that effectively reduced the purchase price by several hundred million dollars. IBEW Exh. 1.0, 9:152-153. That revised transaction ultimately won approval, over IBEW's continued objection because of remaining financial concerns.[21] But there is no question that the renegotiated transaction was considerably more protective of the financial health of the acquiring company and of the public than was the original transaction.

As we now know, IBEW was correct in that case. Even the revised deal was not sufficient to ensure a financially healthy acquirer. FairPoint has filed for bankruptcy and several of the benefits and conditions imposed by the state utility commissions are in jeopardy of being eliminated or substantially modified. IBEW Exh. 1.0, 25-26:455-488; IBEW Exh. 3.0, 17-18:323-363.

In this case, the Proposed Order correctly notes the similarities between the FairPoint transaction and the current case. Based on the current structure of the deal, the ALJ properly found that the transaction was just too risky, and that Frontier was too financially unstable, for the Commission to approve the transaction. IBEW agrees and urges the Commission to adopt the Proposed Order and reject the proposed transaction.

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[20] *Joint Petition of Verizon New England Inc., d/b/a Verizon Vermont and FairPoint Communications, Inc.*, Docket No. 7270 (Vt. PSB, Dec. 21, 2007), available at <http://psb.vermont.gov/sites/psb/files/orders/7270finalorder.pdf>.

[21] *Joint Petition of Verizon New England Inc., d/b/a Verizon Vermont and FairPoint Communications, Inc.*, Docket No. 7270 (Vt. PSB, Feb. 15, 2008), available at < http://psb.vermont.gov/sites/psb/files/orders/2008/7270 final re modified plans_APR.pdf>.

## V. Conclusion

For the reasons set forth above, in its Main Brief, and in the testimony of its witnesses, the International Brotherhood of Electrical Workers Locals 21, 51, and 702 respectfully request the Illinois Commerce Commission to adopt the Proposed Order as its Order in this case, thereby denying the application and rejecting the proposed transaction because it is not in the public interest.

Respectfully submitted,

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Certificate of Service (Docket No. 09-0268)

The undersigned certifies that a copy of the *Brief in Reply to Exceptions of the International Brotherhood of Electrical Workers, Locals 21, 51, and 702 (Public Version)* was served upon the following persons by e-mailing a copy of same this 25th day of March, 2010.

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